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SUBJECT: ICELAND CENTRAL BANK CRISIS: ODDSSON'S NAILS FLAG TO MAST

1. (SBU) SUMMARY. Iceland Central Bank's Chairman of the Board of Governors, David Oddsson, refused Prime Minister Johanna Sigurdardottir's request to resign on Sunday. The Prime Minister made her request by letter of February 2, pending passage of a law allowing the government to dismiss the three governors. The two other Board governors, Ingimundur Fridriksson and Eirikur Gudnason, also received letters. Mr. Gudnason followed Mr. Oddsson and refused to resign, while Fridriksson agreed to step down. The Prime Minister expressed extreme disappointment with Oddsson's decision, stating that the people of Iceland need new leadership in order to restore trust in the Central Bank. END SUMMARY

PM Calls for Central Bank Directors to Resign

2. (SBU) PM Johanna Sigurdardottir sent a letter to the three Central Bank governors on February 2, asking them to hand in their resignations by February 6. In the letter, the Prime Minister stated her desire to replace the Central Bank Board with a single new director under a proposed law reorganizing the structure and management of the Bank. The new bill, to be considered by Parliament shortly, would replace the tripartite board with a single director, appointed by the Prime Minister for a seven-year term. The Director position would be publically advertised and filled with an experienced banking professional with at least a master's degree in economics (Oddsson is a professional politician with no economics education).

3. (SBU) In addition, the proposed legislation would create a new Monetary Policy Committee within the Bank. The Monetary Policy Committee would be comprised of five members: the Governor of the Central Bank, who would chair the committee, two of the Bank's executives responsible for formulating and implementing monetary policy, and two experts appointed by the Governor with the endorsement of the Prime Minister. The Monetary Policy Committee would make all decisions on the Bank's monetary policy control mechanisms.

4. (SBU) On February 6, Ingimundur Fridriksson sent his response stating his intention to resign. Eirikur Gudnason declared his intention to stay on. David Oddsson waited to February 8 to announce his decision to stay on, when a copy of his response letter to the Prime Minister was made public on the Central Bank of Iceland's website.

David's Response: I Won't Go

5. (SBU) David's Oddsson's response to the Prime Minister was a scathing rebuttal to her request. He said her letter was threatening, and accused the governing coalition of misconduct and biased conclusions. Oddsson claims that he and the Central Bank Board of Governors were among the first to warn of the impending banking collapse, and pointed the finger at unnamed ministers whose motive for getting Oddsson out of the Bank is personal vengeance rather than "substantive fault with (his) work." Leaving little doubt as to his intentions, Oddsson defiantly concludes, "For my part, I have never abandoned any task that I have agreed to take on, and I do not intend to do so now."

¶6. (SBU) On Sunday evening, the PM of Iceland issued a statement in response to Oddsson's letter, stating that Oddsson clearly did not share the government's opinion that appointing new employees to the Central Bank would increase the people's faith in the system. She also stated her hope that the bill on the reorganization of the Central Bank would be passed quickly by Parliament.

Legal Authority for Dismissal Unclear

¶7. (SBU) The Prime Minister's legal recourse is unclear. There is no custom or precedent to fire Central Bank governors. Under the Law on the Central Bank on Iceland (2001), and according to the Law on the Rights and Duties of Civil Servants, however, it is possible for a governor to be "dismissed temporarily" if he has not been punctual, or has shown other negligence, disobedience to a legal request or prohibition from his superior, ignorance, or carelessness on the job. In addition, he can be "dismissed temporarily" if he has shown unsatisfactory results, has been inebriated on the job or his behavior or actions [on the job] has otherwise been considered improper, inappropriate, or irreconcilable with the job. It remains to be seen if the Prime Minister will try to use existing statutes to fire Oddsson immediately or wait until the Parliament's near certain passage of the new Central Bank law.

¶8. (SBU) COMMENT. Many believe the Prime Minister will wait until the new Central Bank legislation is enacted. The new legislation would automatically make the Bank Board positions redundant. Iceland's public continues to demand accountability and express their strong desire to clean house. Editorials wonder why Oddsson refuses to leave when his very presence in the Central Bank does nothing but harm the international standing of the tattered Icelandic financial sector. Oddsson may believe he played no role

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in the economic crash, but many Icelanders (and much of the international economic press) hold the Bank - and Oddsson in particular - responsible for not curbing the banks. Meanwhile, the public bickering between the Prime Minister and the Central Bank Director has done little to shore up international investor confidence in the country. It is still an open question whether Oddsson has the political backing from the old guard Independence Party to withstand the demand of the public and government to step down. Demonstrators, fresh from bringing down the previous government, have assembled again in front of the Bank. END
COMMENT.
Van Voorst